



State of Arizona
Department of Education

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MEMORANDUM

To: Sponsors of the National School Lunch Program, School Breakfast Program, and Special Milk Program

From: Mary Szafranski, Deputy Associate Superintendent
Arizona Department of Education, Health & Nutrition Services

Nicholas Dunford, Operations Director
Arizona Department of Education, Health & Nutrition Services

Date: May 4, 2011

RE: Reaffirming the Requirement that School Food Authorities Comply with Federal Regulations Affecting Rebates, Discounts, and Other Applicable Credits in All Cost Reimbursable Contracts

Original Signed

Please be aware that the original policy memorandum from October 21, 2010, (CN# 08-11) has been revised. This policy memorandum supersedes the previous version CN# 08-11, as changes have been made to correct a regulatory citation and for clarification purposes.

This is a reminder to School Food Authorities (SFA) of the importance of ensuring compliance with the procurement requirements established in regulations affecting the National School Lunch Program (NSLP), School Breakfast Program (SBP), and Special Milk Program (SMP) which became effective on November 30, 2007 and emphasize that:

- all cost reimbursable contracts (including contracts with cost reimbursable provisions) require provisions which limit the use of the nonprofit school food service account to pay only for allowable costs—those costs net of all discounts, rebates and other applicable credits;
- all cost reimbursable contracts were to be in compliance with the regulatory requirements by School Year 2009-2010;

- the State Agency (SA) may impose a pre-issuance requirement on a SFA's proposed procurement; and
- the SA must annually review each contract (including supporting documentation) between each SFA and Food Service Management Company (FSMC) before execution of the contract.

Provisions Required in Cost Reimbursable Contracts (including contracts with cost reimbursable provisions)

The regulations at 7 CFR 210.21(f), 215.14a(d), and 220.16(e) require that SFAs must include in all cost reimbursable contracts, in all contracts which include cost reimbursable provisions and in all solicitations for such contracts, provisions which limit the use of nonprofit school food service account funds to costs resulting from proper procurements and contracts. Specifically, the regulations require that SFAs use nonprofit school food service account funds to pay only for allowable costs – those costs net of all discounts, rebates and other applicable credits.

Implementation Timeline

The regulations apply to all new solicitations issued on or after the regulation's effective date, November 30, 2007. Recognizing that a requirement to rebid all contracts immediately would have posed a potential hardship on some SFAs, the Food and Nutrition Service (FNS) included an implementation timeline in the regulation's preamble to structure rebidding of contracts by SFAs in phases. In addition, FNS responded to concerns raised by State Agencies related to cost reimbursable contracts which at the time of the regulation's effective date, included provisions requiring that all discounts, rebates and other applicable credits would be credited to the SFA by the vendor, most often a FSMC. FNS advised that if a solicitation and resulting cost reimbursable contract required all discounts, rebates, and other applicable credits to be credited to the SFA by the FSMC, and the FSMC was crediting all such discounts, rebates and other applicable credits to the SFA under those cost reimbursable contracts, then the relevant cost reimbursable contract could have been amended to incorporate the required language of the regulation without constituting a material change. Based on this timeline, FNS required that all cost reimbursable contracts between an SFA and a FSMC or other vendor, regardless of the date entered into, were to be in compliance with the regulatory requirements by School Year 2009 - 2010.

State Agency Review of Contracts

The regulations allow for two (2) approaches to SA oversight of SFA contracts. The first approach, pre-issuance review requirement, is at the discretion of the SA. The second approach, annual review and approval of each contract between the SFA and FSMC, is required of the SA.

Pre-issuance Review Requirement

The regulations allow a SA to impose a pre-issuance review of an SFA's proposed procurement. 7 CFR 210.21(c), 215.14a(c) and 220.16(c).

Annual Review and Approval of Each Contract between SFA and FSMC

The program regulations for NSLP and SBP require that each SA annually review and approve each contract between any SFA and FSMC before execution of the contract by either party. 7 CFR 210.16(a)(10), 210.19(a)(6) and 220.7(d)(1). Additionally, the program regulations for NSLP require that each SA annually review all supporting documentation to a contract (i.e., solicitation documents, responses submitted by bidders, etc.) between any SFA and FSMC before execution of the contract by either party. 7 CFR 210.19(a)(6). The program regulations for SMP do not explicitly state that each SA must annually review and approve each contract between any SFA and FSMC before execution of the contract by either party, and the program regulations for SMP and SBP do not explicitly state that each SA must annually review all supporting documentation to a contract between any SFA and FSMC before execution of the contract by either party. However, please be aware that it is unlikely for any SFA to contract with an FSMC for solely SMP or SBP without also contracting for NSLP; therefore, each SA is required to annually review each contract (including all supporting documentation) between any SFA and FSMC before execution of the contract by either party if the resulting contract is for NSLP and either the SMP or SBP. In the rare circumstance where the contract between any SFA and FSMC is for SMP and/or SBP, we advise that it is prudent for the SA to annually review each contract (including supporting documentation) before the contract is executed by either party.

Identification of Allowable and Unallowable Costs on Invoices

As noted in prior guidance, the regulations require contractors under cost reimbursable contracts to provide sufficient information to permit the SFA to identify allowable and unallowable costs, as well as the amount of all such discounts, rebates and other applicable credits on invoices and bills presented for payment to the SFA. 7 CFR 210.21(f), 215.14a (d) and 220.16(e). Please review the above cited regulations as they prescribe in detail the information a contractor must provide to an SFA.

The regulations ensure that SFAs receive the full benefit of any discounts, rebates or other applicable credits arising from purchases made under cost reimbursable contracts on behalf of the school meals programs. As such, it helps ensure that limited school meals program resources are used as efficiently as possible.

It is critically important not only that all cost reimbursable contracts include the required provisions as described above, but that the contract provisions are monitored and enforced by SAs. SAs should continue to work closely with SFAs to ensure that cost reimbursable contracts, contract provisions, and solicitations contain the required provisions, as well as, the terms and conditions to accomplish the necessary tracking of the discounts, rebates, and other applicable credits.

If you have any questions or concerns regarding this memo, please contact the Contracts Management Officer, Ellen Pimental at (602) 542-6208 or email at Ellen.Pimental@azed.gov.